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**DAVID KAYNE**

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF CALIFORNIA  
SAN JOSE DIVISION -- E-FILING

DAVID KAYNE, an individual citizen of Georgia, ) Case No. C 07-4721 JF (RS)

Plaintiff, ) **MOTION FOR TEMPORARY**

VS.

THE THOMAS KINKADE COMPANY,  
formerly known as MEDIA ARTS  
GROUP, INC., a Delaware Corporation.

Defendant.

Case No. C 07-4721 JF (RS)

**NOTICE OF MOTION AND  
MOTION FOR TEMPORARY  
RESTRAINING ORDER AND  
PRELIMINARY INJUNCTION;  
BRIEF IN SUPPORT OF MOTION**

**Hearing Date:** October 5, 2007  
**Time:** 9:00 a.m.  
**Courtroom:** 3, 5<sup>th</sup> Floor

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PLAINTIFF'S MOTION AND BRIEF IN SUPPORT  
OF T.R.O AND PRELIMINARY INJUNCTION

CASE NO. C 07-4721 JF (RS)

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**DAVID KAYNE**

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF CALIFORNIA  
SAN JOSE DIVISION -- E-FILING

**Notice of Motion: TO DEFENDANT THE THOMAS KINKADE COMPANY ("TKC") AND ITS ATTORNEYS OF RECORD: PLEASE TAKE NOTICE THAT**, on October 5, 2007 at 9:00 a.m., or as soon thereafter as counsel may be heard by the Court, at Courtroom 3 (5<sup>th</sup> floor) of the United States Courthouse in San Jose, which is located at 280 South 1<sup>st</sup> Street, San Jose, California, 95113, plaintiff David Kayne will (and hereby does) move for the

<sup>1</sup> Pursuant to Local Rule 6-3 and the accompanying separate Motion To Shorten Time, plaintiff is seeking a hearing of this matter on October 5, 2007, or on such other date as the Court may set between now and October 15, 2007. This motion seeks to enjoin defendant from proceeding with an "expedited arbitration" hearing set to occur on October 16, 2007, in which plaintiff would be precluded from calling any witnesses or conducting discovery.

1 following relief: A temporary restraining order and preliminary injunction enjoining  
 2 TKC from proceeding further with, and from attending, the October 16, 2007  
 3 arbitration presently pending before the American Arbitration Association, entitled  
 4 *The Thomas Kinkade Company v. David Kayne* (AAA No. 74-181-E-000733-06), or  
 5 any other arbitral proceeding pursuant to the "expedited" arbitration procedure set  
 6 out in Exhibit "A" to plaintiff's complaint herein, until further order of this Court.  
 7 **PLEASE TAKE FURTHER NOTICE** that this motion is and will be based on the  
 8 following accompanying pleadings filed concurrently with this Notice, together with  
 9 such responsive and reply pleadings as may hereafter be filed, the Complaint on file  
 10 herein, and such other matters as may properly come before the Court at or in  
 11 connection with the hearing of this motion: (1) The brief memorandum of points and  
 12 authorities that follows this notice; (2) The Declaration of David Kayne in support  
 13 of this motion and exhibits attached thereto; (3) The Declaration of Charles L.  
 14 Coleman, III in support of this motion and exhibits attached thereto; (4) The  
 15 Certificate of Service of the summons, complaint and other documents (Local Rule  
 16 5-6); (5) The [Proposed] Temporary Restraining Order; (6) The [Proposed]  
 17 Preliminary Injunction; (7) The accompanying Motion To Shorten Time for hearing  
 18 of this motion (Local Rule 6-3); (8) The Declaration of Charles L. Coleman, III in  
 19 support of the Motion To Shorten Time; and (9) The [Proposed] Order Shortening  
 20 Time to respond to this motion.

21 **Statement of Relief Requested:** By this motion and the accompanying  
 22 Motion To Shorten Time, plaintiff David Kayne ("Mr. Kayne") seeks a temporary  
 23 restraining order and preliminary injunction to prevent defendant TKC from  
 24 proceeding further with a purported "expedited" arbitration procedure under which  
 25 it is seeking to conduct an arbitration "hearing" without affording Mr. Kayne the  
 26 right to call witnesses or conduct discovery, even though Mr. Kayne disputes TKC's  
 27 claim and even though TKC's claim is for an amount in excess of \$1.15 million. As

1 is more fully set out below, Mr. Kayne submits that TKC's purported "expedited"  
 2 arbitration clause is unconscionable and violative of the principles recently  
 3 announced in *Nagrampa v. Mailcoups, Inc.*, 469 F.3d 1257 (9th Cir. 2006) (*en banc*),  
 4 *Davis v. O'Melveny & Myers LLC*, 485 F.3d 1066, 1071 (9<sup>th</sup> Cir. 2007) and other  
 5 recent cases holding that it is for the courts to determine whether an arbitration  
 6 clause is unconscionable. For the reasons set out below and in the accompanying  
 7 declarations, the "expedited" arbitration procedure that TKC seeks to implement on  
 8 October 16, 2007 is unconscionable and should be enjoined.

9 **MEMORANDUM OF POINTS AND AUTHORITIES**

10 **I. STATEMENT OF ISSUES TO BE DECIDED:**

11       A. **Unconscionable "arbitration" clause:** Whether the "expedited"  
 12 arbitration procedure described in an "Application for Credit" drafted by TKC is  
 13 unconscionable under the standards recently articulated in *Nagrampa v. Mailcoups,*  
 14 *Inc.*, 469 F.3d 1257 (9th Cir. 2006) (*en banc*) and other recent cases, where: (a) The  
 15 "Application for Credit" and accompanying "Personal Guaranty" was a contract of  
 16 adhesion presented to Mr. Kayne in circumstances giving rise to procedural  
 17 unconscionability; (b) In presenting its agreements to plaintiff David Kayne, TKC  
 18 was required to, but did not, comply with the disclosure requirements of California  
 19 and federal franchise laws; (c) The AAA "expedited" arbitration procedure  
 20 referenced in TKC's agreement was designed and intended for disputes less than  
 21 \$75,000, whereas TKC now seeks to use this procedure to demand over \$1.15  
 22 million from Mr. Kayne; (d) TKC's standard arbitration agreement even purports to  
 23 further restrict Mr. Kayne's hearing rights beyond what is contemplated in the AAA  
 24 "Expedited" Rules for disputes less than \$10,000 by providing that no discovery may  
 25 be conducted and that the parties "*waive all right to any hearing requiring witness*  
 26 *production*"; (e) TKC's agreement would require that Mr. Kayne (a small business  
 27 owner located in the Buford, Georgia with no businesses in California) to defend

1 against TKC's "expedited" arbitration hearing in Santa Clara County, California;  
 2 and (f) Mr. Kayne would not be able to present his defenses to TKC's claims without  
 3 discovery or the right to call and cross-examine live witnesses. [Answer: YES].

4       **B. TKC's Anticipated Defenses:** Plaintiff anticipates that TKC's  
 5 defenses to his claims will seek to divert attention from the clear unconscionability  
 6 of its "expedited" arbitration clause by focusing instead on the following issue  
 7 expected to be raised in TKC's anticipated motion due to be filed on October 4, 2007:  
 8 Whether Mr. Kayne is somehow precluded, by virtue of having contended (in  
 9 separate proceedings before Judge Pannell of the U.S. District Court for the  
 10 Northern District of Georgia) that no agreement *was ever formed* between TKC and  
 11 Mr. Kayne that included an arbitration provision where: (a) The question of  
 12 whether Mr. Kayne formed an agreement with TKC (issues of offer, acceptance and  
 13 consideration) is *separate* from whether the arbitration clause in that agreement is  
 14 or was *unconscionable*; (b) Mr. Kayne's complaint expressly disavows any intention  
 15 to "re-litigate" the issues presented to Judge Pannell; and (c) In any event, the  
 16 Ninth Circuit's *en banc* decision in *Nagrampa* was not issued until *after* Mr. Kayne  
 17 had presented is other arguments (based on pre-*Nagrampa* law) to Judge Panel.  
 18 [Answer: NO.]

19       **C. Balancing of Harm for Purposes of Injunctive Relief:** Whether  
 20 plaintiff David Kayne's motion for a temporary restraining order and preliminary  
 21 injunction should be granted where: (a) Plaintiff has a strong case on the merits,  
 22 based on *Nagrampa* and the circumstances, terms and effect of TKC's arbitration  
 23 clause; (b) Mr. Kayne faces possible irreparable harm if TKC is permitted to pursue  
 24 its "expedited" arbitration "hearing" on October 16; (c) TKC, by contrast, will suffer  
 25 no apparent harm if it is required to wait a few more days or weeks before pursuing  
 26 its purported claim against Mr. Kayne (which allegedly arose in 2002) in an  
 27 appropriate forum (a court) and under appropriate rules providing minimum due

1 process rights to Mr. Kayne; and (d) The requested injunctive relief will simply  
 2 preserve the *status quo* so that this Court can consider and rule on Mr. Kayne's  
 3 complaint before the TKC "arbitration" occurs. [Answer: YES.]

4 **II. STATEMENT OF RELEVANT FACTS**

5 **A. Summary of Relief Requested:**

6 Plaintiff David Kayne ("Mr. Kayne") seeks a temporary restraining order and  
 7 preliminary injunction to prevent defendant The Kinkade Company ("TKC") from  
 8 enforcing an unconscionable and unlawful "expedited" arbitration provision  
 9 contained in certain franchise agreement documents signed by Mr. Kayne.

10 The Complaint does not seek to contest the validity or enforceability of TKC's  
 11 "Application for Credit" and "Personal Guaranty" documents in their entirety.  
 12 Instead, it asserts that the arbitration provision set out in the "Application for  
 13 Credit" (which TKC seeks to apply through the "Personal Guaranty") is  
 14 unconscionable, and therefore unenforceable, under the standards recently  
 15 articulated in the Ninth Circuit's *en banc* decision in *Nagrampa v. Mailcoups, Inc.*,  
 16 469 F.3d 1257 (9th Cir. 2006) ("Nagrampa"). The provisions at issue here – which  
 17 would require Mr. Kayne to travel across the United States to try to defend against  
 18 a claim for over \$1.15 million in a forum where he has no right to call and cross-  
 19 examine witnesses or conduct discovery – clearly are unconscionable under  
 20 *Nagrampa* and other recent decisions. *See* the Complaint on file herein and the  
 21 Declaration of David Kayne ("Kayne Dec.") verifying the factual allegations of the  
 22 Complaint. *See also*, the Declaration of Charles L. Coleman ("Coleman Dec.")  
 23 accompanying this memorandum, authenticating various documents in this matter.

24 Because TKC intends to proceed with the October 16 arbitration "hearing" in  
 25 the absence of injunctive relief from this Court, Mr. Kayne seeks either: (a) A  
 26 temporary restraining order preventing Mr. Kayne from proceeding further with  
 27 the arbitration, coupled with an expedited hearing on a preliminary injunction

1 within ten (10) days thereafter; or (b) If a temporary restraining order is not issued,  
 2 a preliminary injunction to be issued based on a hearing to be conducted on October  
 3 5, 2007 (based on TKC's anticipated October 4 motion filing), or on such other date  
 4 as the Court may determine on or before October 15, 2007 (the day before TKC's  
 5 "expedited" arbitration is set to occur).

6 **B. Background Facts**

7 David Kayne ("Mr. Kayne") is the founder, President and (along with his  
 8 wife, Tracy) the principal shareholder of his family owned art gallery, Kayne Art  
 9 Galleries of Georgia, Inc. ("KAG"), a Georgia Corporation. Complaint, ¶ 9; Kayne  
 10 Dec., ¶¶ 3, 4. KAG was founded in order to market Thomas Kinkade art work and  
 11 reproductions in the Atlanta area. *Id.* The Thomas Kinkade Company ("TKC")  
 12 controls, distributes, and markets Thomas Kinkade artwork and TKC-  
 13 manufactured reproductions through a nationwide network of dealers. Complaint,  
 14 ¶ 10; Kayne Dec., ¶ 3. The authorized dealers are categorized based on the volume  
 15 of artwork and TKC-manufactured reproductions the dealer would purchase from  
 16 TKC to sell to customers. *Id.*

17 Mr. Kayne was encouraged by TKC to become a TKC authorized dealer of the  
 18 highest level, a "Signature Dealer." Complaint, ¶ 11; Kayne Dec., ¶ 3. As an  
 19 enticement to sign up as a "Signature Dealer," TKC offered Mr. Kayne, and other  
 20 potential dealers of this level, exclusive territories in which to sell the products,  
 21 exclusive marketing opportunities, incentives such as cash and prizes, and other  
 22 purported benefits. *Id.* These inducements were explained and offered to those who  
 23 attended TKC's motivational "training" sessions. Mr. Kayne attended one such  
 24 "training" session at TKC's headquarters in Santa Clara County, California, where  
 25 TKC encouraged and induced Mr. Kayne to become a "Signature Dealer."  
 26 Complaint, ¶¶ 12-13; Kayne Dec., ¶ 3.

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1 TKC represented to Mr. Kayne and other prospective and actual dealers that  
2 the company adhered to certain "Christian values" of Thomas Kinkade and further  
3 represented to Mr. Kayne and other dealers that they would be dealing with TKC in  
4 an atmosphere of mutual trust and respect. Complaint ¶12; Kayne Dec., ¶ 3. TKC  
5 often referred to its dealers as its "partners." *Id.* Based on representations  
6 regarding the company's "trustworthiness," Mr. Kayne refrained from scrutinizing  
7 the agreement documents to the extent he normally would have in other business  
8 ventures. *Id.*

9       Based on TKC's representations, Mr. Kayne was induced to sign, and did sign  
10 on behalf of KAG, a series of standard form "Dealer Agreements" prepared by TKC  
11 (then operating as "Media Arts Group, Inc."). Complaint, ¶12 and Exhibit "B"  
12 thereto; Kayne Dec., ¶3. The Dealer Agreements required KAG to purchase at least  
13 \$100,000 of art inventory per dealer location from TKC in the first year of the  
14 agreements and also required an achievement of at least \$200,000 in retail sales per  
15 dealer location in the first year. Both of these requirements were subject to  
16 adjustment in later years "according to a formula applied to every Signature  
17 Gallery." Complaint, ¶ 13 and Exhibit "B"; Kayne Dec., ¶ 3.

18 TKC and KAG entered into Dealer Agreements in 1999-2000. Complaint,  
19 ¶14; *Kayne* Dec., ¶ 3. In or about October 2001, after the Dealer Agreements were  
20 entered into, TKC presented Mr. *Kayne* with TKC's standard form "Application for  
21 Credit" (hereinafter "Application") and "Personal Guaranty" (hereinafter  
22 "Guaranty"). *Id.*; Complaint, Exhibit "A". Embedded in the Application and  
23 referred to by reference in the Guaranty is the "expedited" arbitration provision  
24 that TKC now seeks to apply against Mr. *Kayne*, and which is the subject of the  
25 Complaint in this case. *Id.* The "expedited arbitration" provision states:

1 DISPUTES: ANY DISPUTE OR CONTROVERSY ARISING FROM THIS  
 2 AGREEMENT WILL BE RESOLVED BY ARBITRATION BY THE  
 3 AMERICAN ARBITRATION ASSOCIATION AT SANTA CLARA COUNTY,  
 4 CALIFORNIA. THE LANGUAGE OF THE ARBITRATION SHALL BE  
 5 ENGLISH. THE NUMBER OF THE ARBITRATORS SHALL BE ONE.  
 6 THE PARTIES AGREE THE AMERICAN ARBITRATION ASSOCIATION'S  
 7 EXPEDITED RULES SHALL APPLY AND **THEY WAIVE ALL RIGHT TO**  
**ANY HEARING REQUIRING WITNESS PRODUCTION. THE**  
**ARBITRATOR SHALL ISSUE AN AWARD BASED UPON THE**  
**WRITTEN DOCUMENTARY EVIDENCE SUPPLIED BY THE**  
**PARTIES.** THE ARBITRATOR'S AWARD SHALL BE BINDING AND  
 8 FINAL. THE LOSING PARTY SHALL PAY ALL ARBITRATION  
 9 EXPENSES, INCLUDING ALL ATTORNEY'S FEES. *[Italics and bold*  
*added].*

10 *Id.* The "Personal Guaranty", which accompanied the Application, states that "[a]s  
 11 Guarantor, [Mr. Kayne] is also bound by the above arbitration clause." *Id.*

12 TKC is a California-based business that is subject to the California Franchise  
 13 Investment Law (Cal. Corps. Code §§ 31000, *et seq.*) and corresponding federal  
 14 regulations promulgated by the Federal Trade Commission (46 C.F.R. Part 436),  
 15 but KAG never provided the required disclosures to Mr. Kayne or his family-owned  
 16 company (Kayne Art Galleries of Georgia, Inc., or "KAG"); had it done so, Mr. Kayne  
 17 would not have signed the "Personal Guaranty" or the "Application for Credit" *See*  
 18 Complaint, ¶¶ 15-29; Kayne Dec., ¶ 3.

19 After Mr. Kayne was induced to have KAG become a Signature Dealer and to  
 20 subsequently sign the KAG "Application for Credit" and accompanying "Personal  
 21 Guaranty", the relationship between TKC and KAG (and Mr. Kayne) soured. The  
 22 relationship between the parties deteriorated because the high volume art business  
 23 that TKC required and encouraged its Signature Dealers (including KAG) to  
 24 develop proved to be increasingly unprofitable. Complaint, ¶ 33; Kayne Dec., ¶ 3.  
 25 KAG and other Signature Dealers became disillusioned with the business model  
 26 that had been sold to them by TKC without adequate and detailed disclosures. *Id.*  
 27 The parties then engaged in a series of legal disputes in which TKC pursued KAG,  
 28 and Mr. Kayne personally, for debts allegedly resulting from KAG's inability to sell

1 the large volume of TKC artwork required under TKC's "Signature Dealer"  
 2 agreements.<sup>2</sup>

3       Nearly five years after Mr. Kayne signed the "Personal Guaranty," TKC filed  
 4 a demand for arbitration with the American Arbitration Association, invoking the  
 5 "expedited" arbitration procedures set out the Application and referred to by  
 6 reference in the Guaranty. Kayne Dec., ¶¶ 3, 8 and Exhibit 2 thereto (Arbitration  
 7 demand). TKC thereafter increased and supplemented its claim to over \$1.15  
 8 million. Coleman Dec. ¶ 3 and Exhibit 2 thereto. At no time has TKC or its counsel  
 9 indicated that TKC has agreed to waive the draconian limitations on the scope of  
 10 the arbitration it is seeking to conduct under the arbitration clause at issue as set  
 11 out in Exhibit "A" to the Complaint. Declaration of Charles L. Coleman in Support  
 12 of Motion To Shorten Time, ¶ 4. In this motion, Mr. Kayne seeks injunctive relief to  
 13 prevent this unconscionable arbitration clause from being applied against him.

14 **III. ARGUMENT AND LEGAL AUTHORITIES**

15       **A. The District Court Is the Proper Forum for Mr. Kayne's Challenge**  
 16       **to the Enforceability of TKC's Unconscionable Arbitration Clause.**

17       As an initial matter, this Court is the proper venue for a determination of the  
 18 legality of the arbitration provision contained in the Application and allegedly  
 19 incorporated by reference in the Guaranty. The *Nagrampa* decision recently held  
 20 that: "[w]hen the crux of the complaint is not the invalidity of the contract as a  
 21 whole, but rather the arbitration provision itself, then the federal courts must  
 22 decide whether the arbitration provision itself is invalid and unenforceable  
 23 pursuant to 9 U.S. C. § 2 of the FAA." *Nagrampa, supra*, 469 F.3d at 1264. Thus,  
 24 the Court must closely examine the Complaint to determine whether striking the  
 25 arbitration provision may affect the validity of the "Application for Credit" or

27       

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<sup>2</sup> A summary of the parties' legal disputes is set out in the Complaint, ¶¶ 33-44, as  
 28 verified by Mr. Kayne in the Kayne Dec. at ¶ 3.

1 "Personal Guaranty" in their entirety. *See id.* When this is done, it is clear that the  
 2 facially and actually unconscionable "expedited" arbitration clause is severable from  
 3 the remaining terms of these documents. Similarly, in *Davis v. O'Melveny & Myers*  
 4 *LLC*, 485 F.3d 1066, at 1071-1072 (9<sup>th</sup> Cir. 2007), the court relied on *Nagrampa* in  
 5 stating that "whether . . .[the] arbitration clause is unconscionable is for the court to  
 6 decide." Thus, Mr. Kayne's Complaint is filed as a response to TKC's arbitration  
 7 demand because the arbitration clause itself is unconscionable, and this Court is  
 8 the right place to resolve that issue.

9 In response to TKC's effort to enforce its "expedited" arbitration clause, Mr.  
 10 Kayne's Complaint seeks declaratory and injunctive relief only as to the arbitration  
 11 provision and not as to the entirety of the "Application for Credit" and "Personal  
 12 Guaranty". Specifically, in the First Cause of Action, Mr. Kayne seeks a declaration  
 13 that the arbitration provisions of Exhibit A are unlawful, unconscionable,  
 14 unenforceable, and void as a matter of law, so that if TKC wishes to pursue Mr.  
 15 Kayne under the "Personal Guaranty", it must do so in a court of law, in which Mr.  
 16 Kayne will be afforded a full, fair and complete hearing and due process.  
 17 Complaint, ¶ 60. Alternatively, this cause of action requests that, in the event that  
 18 an award or other form of relief is given to TKC by the AAA arbitrator appointed  
 19 pursuant to Exhibit "A", David Kayne be entitled to a declaration that any such  
 20 award is unenforceable and void. Complaint, ¶ 61.

21 In his Second Cause of Action, Mr. Kayne asserts that TKC should be  
 22 preliminarily and permanently enjoined from pursuing this or any other arbitration  
 23 under the provisions of Exhibit "A", and (if necessary) enjoined from seeking to  
 24 enforce any arbitral award against Mr. Kayne that it might obtain in connection  
 25 with Exhibit "A". Complaint, ¶ 64. In the Third Cause of Action, Mr. Kayne seeks a  
 26 declaration that TKC's attempt to enforce the "expedited" arbitration provisions of  
 27 Exhibit A, or any award issued as a result thereof, is an "unlawful, unfair or

1 fraudulent business act or practice" within the meaning of California Unfair  
 2 Competition Law. Complaint at ¶ 68. The Fourth and final Cause of Action  
 3 requests a preliminary and permanent injunction enjoining TKC from pursuing this  
 4 or any other arbitration under the provisions of Exhibit "A", as said provisions are  
 5 unlawful and violate the California Unfair Competition Law as applied to Mr.  
 6 *Kayne*. Complaint, ¶¶ 70-71. In this regard, Mr. *Kayne*'s request for an injunction  
 7 under the Unfair Competition Law is not subject to arbitration where it serves a  
 8 public purpose. *Cruz v. Pacificare Health Systems, Inc.*, 30 Cal. 4th 303, 316 (2003).

9 Thus, because Mr. *Kayne* does not challenge or threaten in this proceeding to  
 10 invalidate the contract as a whole, but rather, challenges the legality of the  
 11 arbitration provision itself, *Nagrampa* instructs that this Court is "required to turn  
 12 to California law to address [Mr. *Kayne*'s] arguments regarding the  
 13 unconscionability of the arbitration provision." *See Nagrampa, supra*, 469 F.3d at  
 14 1271.

15 **B. Standard of Review**

16 The Ninth Circuit's well-established standard for a preliminary injunction  
 17 requires that the moving party show either (1) a combination of probable success on  
 18 the merits and the possibility of irreparable injury, or (2) that serious questions are  
 19 raised and the balance of hardships tips sharply in favor of the moving party.<sup>3</sup>  
 20 *Stuhlbarg Int'l Sales Co., Inc. v. John D. Brush and Co., Inc.*, 240 F.3d 832, 839-40  
 21 (9th Cir. 2001) (internal citation omitted); *see also Arcamuzi v. Continental Air*  
 22 *Lines, Inc.*, 819 F.2d 935, 937 (9th Cir. 2001). These standards are not two separate  
 23 tests but, rather, outer reaches of a single continuum. *Stuhlbarg International*  
 24 *Sales Co., supra*, 240 F.3d at 840; *International Jensen, Inc. v. Metrosound U.S.A.*, 4  
 25

26 <sup>3</sup> Courts often also consider whether the public interest favors the issuance of the  
 27 injunction. *See Southwest Voter Registration Ed. Project v. Shelley*, 344 F.3d 914,  
 917-18 (9th Cir. 2003).

1 F.3d 819, 822 (9th Cir. 1993). They represent two points on a sliding scale in which  
 2 the degree of irreparable harm increases as the probability of success on the merits  
 3 decreases. *Big Country Foods, Inc. v. Board of Education*, 868 F.2d 1085, 1088 (9th  
 4 Cir. 1989).

5 As set forth in detail below, Mr. Kayne meets either prerequisite and should  
 6 be granted a preliminary injunction to prevent TKC from pursuing arbitration  
 7 under an unconscionable and unenforceable arbitration provision.

8 **C. There Is a Strong Likelihood That Mr. Kayne Will Succeed on the**  
 9 **Merits of His Complaint**

10 Mr. Kayne is required only to demonstrate the "irreducible minimum" that he  
 11 has a "fair chance of success on the merits" of his case. *Johnson v. California State*  
 12 *Board of Accountancy*, 72 F.3d 1427, 1429-30 (9th Cir. 1995); *see also Republic of the*  
 13 *Philippines v. Marcos*, 862 F.2d 1355, 1362 (9th Cir. 1988). It is well-established  
 14 that unconscionability is a generally applicable contract defense, which may render  
 15 an arbitration provision unenforceable. *Nagrampa, supra*, 469 F.3d at 1280  
 16 (internal citation omitted). California courts have extended the doctrine of  
 17 unconscionability to embrace franchise agreements. *Id.* at 1280. California law is  
 18 applied law to determine whether the arbitration provision at issue here is  
 19 unconscionable. *See id.*

20 In determining whether an agreement to arbitrate is "unconscionable" and  
 21 hence unenforceable, the prevailing California view is that a sliding scale should be  
 22 invoked whereby if strong evidence of procedural unconscionability is presented,  
 23 less evidence is necessary with respect to substantive unconscionability, and vice-  
 24 versa. *Nagrampa, supra*, 469 F.3d at 1280; *Gentry v. Superior Court.*, 42 Cal.4<sup>th</sup>  
 25 443, 64 Cal. Rptr. 3d 773, 793 (2007). There is strong evidence that the "expedited"  
 26 arbitration provision at issue here is both procedurally and substantively

27

28

1 unconscionable, and will ultimately be declared void and unenforceable under  
 2 California law. *See* Complaint and Kayne Dec., ¶ 3.

3 **1. The Arbitration Provision Is Procedurally Unconscionable**

4 **a. The Arbitration Agreement Is a Contract of Adhesion**

5 The threshold inquiry in California's unconscionability analysis is "whether  
 6 the arbitration agreement is adhesive." *Nagrampa, supra*, 469 F.3d at 1281. An  
 7 adhesive contract is defined as a standardized contract, imposed upon the  
 8 subscribing party without an opportunity to negotiate the terms. *Id.* (citation  
 9 omitted). Standards for procedural unconscionability are satisfied by a finding that  
 10 the arbitration provision was presented on a take-it-or-leave-it basis and that it was  
 11 oppressive due to an inequality in bargaining power that resulted in no real  
 12 negotiation and an absence of meaningful choice. *Id.* Courts have found that  
 13 ordinary contracts of adhesion, although they are indispensable facts of modern life  
 14 that are generally enforced, contain a degree of procedural unconscionability even  
 15 without any notable surprises, and "bear within them a clear danger of oppression  
 16 and overreaching." *Gentry, supra*, 64 Cal. Rptr. at 793 (citation omitted).

17 Here, Mr. Kayne was presented with the arbitration provision embedded in a  
 18 take-it-or leave it, standard contract of adhesion entitled "Application for Credit"  
 19 which was drafted entirely by TKC. Mr. Kayne was provided with no real  
 20 opportunity to negotiate the terms of the arbitration provision. Complaint, ¶¶ 30-31  
 21 Kayne Dec. at ¶ 3. Furthermore, Mr. Kayne, on behalf of KAG, was in a  
 22 substantially weaker bargaining position than TKC.

23 TKC's agreements were part of what was, in fact, a franchise relationship,  
 24 although TKC did not provide the required disclosures. Complaint, ¶¶ 15-29;  
 25 Kayne Dec. ¶ 3. Franchise agreements have some characteristics of adhesion  
 26 because of the "vastly superior bargaining strength" of the franchisor. *See*  
 27 *Nagrampa, supra*, 469 F.3d at 1282 (citation omitted). In addition to KAG's status

as TKC's franchisee, TKC was an existing creditor of KAG, which had signed Dealer Agreements obliging KAG to continue to purchase hundreds of thousands of dollars of TKC's mass-produced reproductions as inventory. Complaint, ¶ 13-14, 30-32.

b. TKC Failed To Make Disclosures to Mr. Kayne as Required by California and Federal Franchise Law.

An important factor in the procedural unconscionability analysis is the manner in which the contract or the disputed clause was presented or negotiated. *Nagrampa, supra*, 469 F.3d at 1282. Procedural unconscionability focuses on the factors of surprise and oppression, with surprise being a function of the reasonable expectations of the weaker party. *Higgins II v. Super. Ct.*, 140 Cal. App. 4th 1238, 1249 (2006); see also *Nagrampa, supra*, 469 F.3d at 1280. Surprise involves the extent to which the supposedly agreed-upon terms of the bargain are hidden in the prolix printed form drafted by the party seeking to enforce the disputed terms *Ferguson v. Countrywide Credit Indus., Inc.*, 298 F.3d 778, 783 (9th Cir. 2002). Oppression arises from an inequality of bargaining power which results in no real negotiation and an absence of meaningful choice. *Id.*

Mr. Kayne has strong evidence of both surprise and oppression. Mr. Kayne was presented with an adhesive contract and was not specifically informed of the existence of the arbitration provision. Kayne Dec., ¶12. The provision is buried in a two page document entitled "Application for Credit," and contains no clear indication or heading regarding an agreement to arbitrate. Complaint, Exh A.; Kayne Dec. ¶ 3. The agreement to arbitrate in the "Personal Guaranty" section is even less conspicuous. Mr. Kayne is supposedly required to submit to the "expedited" arbitration provision contained in the prior section by virtue of a single sentence in the Guaranty: "As Guarantor, I am also bound by the above arbitration clause." This sentence apparently incorporates the preceding "expedited" arbitration provision which includes no signal or heading identifying the provision

1 as an arbitration agreement. Mr. Kayne was certainly surprised, five years after  
 2 signing the document, to learn that not only did KAG agree to arbitrate in a  
 3 particular manner, but that he was personally obligated to do so as well.  
 4 Complaint, ¶ 31, Kayne Dec. ¶3.

5 The arbitration provision also is unduly oppressive due to the manner in  
 6 which it was presented. Specifically, TKC failed to provide applicable disclosures as  
 7 required by California and Federal Franchise laws and regulations, which rendered  
 8 Mr. Kayne unable to make an informed decision regarding the arbitration provision  
 9 itself.

10 Pursuant to the California Franchise Investment Law ("CFIL") set forth in  
 11 California Corporations Code §§ 31000, *et seq.*, TKC was required to, but did not,  
 12 make detailed disclosures to KAG and/or to Mr. Kayne on a wide variety of subjects  
 13 specified in the Uniform Franchise Offering Circular ("UFOC"), prescribed by the  
 14 California Commissioner of Corporations, and pursuant to the CFIL. Complaint,  
 15 ¶¶ 17-18, 21-22; Kayne Dec. ¶ 3. Prior to signing the Application containing the  
 16 "expedited" arbitration provision, neither Mr. Kayne nor KAG received any  
 17 disclosures detailing the financial details of the Dealer Agreement arrangement, the  
 18 Application or the Guaranty. *Id.* At no point in time during the parties'  
 19 relationship did TKC provide Mr. Kayne or KAG with the required disclosures. *Id.*

20 Pursuant to federal franchising regulations (16 C.F.R. Part 436—"Disclosure  
 21 Requirements and Prohibitions Concerning Franchise"), promulgated by the  
 22 Federal Trade Commission ("FTC") under the Federal Trade Commission Act (15  
 23 U.S.C. §§ 41-58), and specifically under 16 C.F.R. Part 536, TKC was required to,  
 24 but did not, make detailed financial disclosures to KAG and/or to Mr. Kayne about  
 25 the Dealer Agreement arrangement as well as the Application and the Guaranty.  
 26 Complaint, ¶¶ 27-29; Kayne Dec., ¶ 3. Notably, "item 17.u" and "17.v" of the  
 27 "Disclosure Items" required under 16 C.F.R. § 436.5 called for explicit disclosures by

1 TKC of the dispute resolution and forum provisions of any agreements it entered  
 2 into with franchisees and their principals. Prior to signing the Application and  
 3 Guaranty containing the "expedited" arbitration agreement, neither Mr. Kayne, nor  
 4 KAG received any disclosures detailing the financial details of the Dealer  
 5 Agreement arrangement, the Application, or the Guaranty contained therein.  
 6 Complaint, ¶¶ 27-29, Kayne Dec. § 3.

7 Thus, the manner in which Mr. Kayne was presented with the "expedited"  
 8 arbitration provision, was procedurally improper and fraught with oppression due  
 9 to the fact that Mr. Kayne was not provided with the disclosures that both federal  
 10 and California law require. These failures prevented Mr. Kayne, as a franchisee in  
 11 a substantially weaker bargaining position and without an opportunity to negotiate,  
 12 from making an informed decision regarding the arbitration provision contained in  
 13 the "Credit Application" and "Personal Guaranty". These franchise-related issues  
 14 merely exacerbated the independently-sufficient procedural unconscionability that  
 15 attended the presentation and execution of the "Application for Credit" and  
 16 "Personal Guaranty".

17 At the time he signed the Application on behalf of KAG and the Guaranty in  
 18 2001, it was not within Mr. Kayne's reasonable expectations that, five or six years  
 19 later, without extending any additional credit to KAG or any separate credit to Mr.  
 20 Kayne, or even manifesting its "acceptance" of the Application, TKC would now  
 21 assert that it is entitled to conduct a "no witness," "no discovery" mini-hearing in  
 22 California that court result in Mr. Kayne facing an award against him personally  
 23 for more than one million dollars. Complaint, ¶ 31, Kayne Dec. ¶ 3.

24 **2. The Arbitration Provision Is Substantively Unconscionable.**

25 An arbitration provision is substantively unconscionable if it is overly harsh  
 26 or generates one-sided results. *Armendariz v. Foundation Health Psychcare*  
 27 *Services Inc.*, 24 Cal. 4th 83, 114 (2000). In this case, the "expedited" arbitration

1 provision heavily favors the drafter, TKC. It states that the parties must agree to  
 2 the AAA's "expedited rules," yet simultaneously requires the franchisee to agree to  
 3 substantive modifications to the rules themselves, without any notice to the  
 4 franchisee as to how the "expedited rules" have been modified. For example, Rule  
 5 E-6 states:

6                   *Where no party's claim exceeds \$10,000, exclusive of interest and arbitration*  
 7 *costs, and other cases in which the parties agree, the dispute shall be*  
 8 *resolved by submission of documents, unless any party requests an oral*  
 9 *hearing, or the arbitrator determines that an oral hearing is necessary. The*  
*arbitrator shall establish a fair and equitable procedure for the submission of*  
*documents. [Italics added].*

10 Coleman Dec., ¶ 2 and Exhibit 1 thereto. The plain language of Rule E-6 indicates  
 11 that the Rule was intended for claims that are less than \$10,000, while the amount  
 12 in controversy here is now over \$1.15 million. Coleman Dec. ¶ 3 and Exhibit 2  
 13 thereto. Similarly, the "expedited" arbitration provision requires a waiver of "all  
 14 right to any hearing requiring witness production," and that the award will be  
 15 based strictly "upon the written documentary evidence supplied by the parties."  
 16 Yet, Expedited Rule 6 clearly states that a party can request an oral hearing, with  
 17 no restrictions as to witness production.

18                   It is a matter of business common sense that the "expedited" documents-  
 19 only rules contemplated by the AAA are intended for commercial disputes between  
 20 merchants where the only question presented is an accounting for invoices and  
 21 receipts in amounts so small as to make it uneconomical to have a full-blown  
 22 hearing on the subject. This is a far cry from the use to which TKC now seeks to  
 23 put the clause that it drafted. TKC seeks over \$1.15 million from a small Georgia  
 24 business owner that hotly disputes TKC's claim and has a number of defenses that  
 25 will be precluded by the application of the "expedited" procedures. Kayne Dec. ¶ 12.

26                   As was foreseeable when it induced people to sign its agreements, TKC's  
 27 provision containing the modified "expedited rules" heavily favors TKC, whose

1 position is simply "pay up and don't argue". No explanation for these restrictions,  
 2 which remove all notion of basic fairness and due process from the proceeding, can  
 3 be found in the documents and no explanation was given orally to Mr. Kayne. *See*  
 4 Complaint, ¶ 31 and Kayne Dec., ¶¶ 3, 12. Similarly, only a legally sophisticated  
 5 party could have possibly understood that the modified "expedited" rules were  
 6 considerably less favorable to Mr. Kayne than those set forth in AAA's Commercial  
 7 Rules designed for million-dollar disputes. Moreover, "even experienced but legally  
 8 unsophisticated businessmen may be unfairly surprised by unconscionable contract  
 9 terms." *Gentry, supra*, 64 Cal. Rptr. at 795 (citing *Stirlen v. Supercuts, Inc.*, 51 Cal.  
 10 App. 4th 1519, 1535 (1997)).

11 The arbitration provision also contains a forum selection clause, which  
 12 requires the arbitration to take place in Santa Clara County, California, TKC's  
 13 principal place of business. Complaint, Exhibit "A"; Kayne Dec. ¶ 3 and Exhibit 1  
 14 thereto. To assess the reasonableness of "place and manner" provisions in an  
 15 arbitration clause, the respective circumstances of the parties are considered.  
 16 *Nagrampa, supra*, 469 F.3d at 1288. Here, the parties' bargaining positions were  
 17 unequal, which resulted in an oppressive contract of adhesion, containing a forum  
 18 selection clause. The forum selection clause requires Mr. Kayne, a citizen of  
 19 Georgia, to travel thousands of miles across the country to California, while TKC  
 20 has a minimal travel burden, if any, as its principal place of business is within the  
 21 same county as the selected forum. Mr. Kayne, along with other small franchisees  
 22 located outside of California, must incur additional traveling and living expenses  
 23 and increased costs associated with having counsel familiar with California law.

24 Similar to the forum selection clause at issue in *Nagrampa*, the forum  
 25 selection clause here "has no justification other than as a means of maximizing  
 26 advantage over [franchisees]." *Nagrampa, supra*, 469 F.3d at 1289-90. TKC could  
 27 have reasonably expected that the selected forum in California would have

1 effectively precluded out of state franchisees, including KAG and Mr. Kayne, from  
 2 asserting claims and defenses against it due to burdens and expenses that the  
 3 forum selection places on small business owners. *See id.* at 1290.

4 Mr. Kayne has presented substantial evidence supporting his claim that the  
 5 arbitration provision is unconscionable. *See* Complaint, Exhibit "A" thereto, and the  
 6 Kayne Dec. As alleged in the Complaint, "an unconscionable contract amounts to  
 7 an unfair business practice under Business and Professions Code Section 17200."  
 8 *See In re First Alliance Mortgage Co.*, 280 B.R. 246, 251 (C.D. Cal. 2002). Thus, Mr.  
 9 Kayne has demonstrated a strong likelihood of success on the merits of the  
 10 Complaint.

11       **D. Mr. Kayne Will Suffer Immediate, Irreparable Injury If**  
 12       **Injunctive Relief Is Denied.**

13       In addition to demonstrating a "fair chance of success" on the merits of his  
 14 Complaint, Mr. Kayne also can demonstrate a significant threat of irreparable  
 15 injury warranting injunctive relief. *See Simula, Inc. v. Autoliv, Inc.*, 175 F.3d 716,  
 16 725 (9th Cir. 1999). Such harm must be immediate or imminent. *Caribbean*  
 17 *Marine Serv. Co. v. Baldridge*, 844 F.2d 668, 674 (9th Cir. 1988); *Midgett v. Tri-*  
 18 *County Metro. Transp. Dist. of Oregon*, 254 F.3d 846, 850-51 (9th Cir. 2001).

19       In this case, TKC has already noticed and demanded the "expedited"  
 20 arbitration. An arbitrator has been appointed, and the "hearing" is set to occur on  
 21 October 16, 2007. Coleman Dec., ¶ 7 and Exhibit 6 thereto. Mr. Kayne is faced  
 22 with the immediate and untenable position of either waiving his *Nagrampa*-based  
 23 objections to the arbitration or succumbing to an unconscionable arbitration  
 24 procedure where he will be forced to forfeit all rights to meaningful discovery,  
 25 witness testimony, and cross-examination in an unfavorable forum. Mr. Kayne has  
 26 several substantial defenses regarding the claims that TKC is asserting against  
 27 him. Kayne Dec., ¶ 12. In order to establish these defenses, however, Mr. Kayne

1 must be allowed the basic due process rights of conducting meaningful discovery,  
 2 calling and cross-examining witnesses. *Id.*

3 If the arbitration is allowed to proceed under the unconscionable arbitration  
 4 provision, Mr. Kayne will be subjected to an arbitration procedure where he will be  
 5 deprived of the right to present an adequate defense. Exhibit A declares that such  
 6 an award would be "binding and final." Accordingly, while Mr. Kayne retains the  
 7 right to challenge any arbitral award resulting from the hearing based on  
 8 *Nagrampa* and other recent case law (such as *Gentry*) dealing with the  
 9 unconscionability of the arbitration clause, he has a significant and legitimate  
 10 interest in determining *before* the arbitration occurs whether it is unconscionable.

11 **E. The Balance of Harms Tips Sharply in Mr. Kayne's Favor.**

12 Where plaintiff shows a strong likelihood of success on the merits and a  
 13 threat of irreparable harm, an order granting a preliminary injunction need not  
 14 reach the balance of hardships. Indeed, "[i]f the balance of harm tips decidedly  
 15 toward the plaintiff, then the plaintiff need not show as robust a likelihood of  
 16 success on the merits as when the balance tips less decidedly. *State of Alaska v.*  
 17 *Native Village of Venetie*, 856 F.2d 1384, 1389 (9<sup>th</sup> Cir. 1988). As demonstrated  
 18 above, Mr. Kayne is highly likely to succeed on the merits of his case, and certainly  
 19 has at least a "fair chance" of success. Even if the Court determines that the  
 20 likelihood of his success is less than "strong" and continues to the balancing of  
 21 hardships analysis, the balance tips decidedly in Mr. Kayne's favor.

22 **1. TKC Will Suffer Little or No Irreparable Harm if A**  
 23 **Preliminary Injunction is Granted**

24 In contrast to the immediate and irreparable harm Mr. Kayne will suffer  
 25 should the "expedited" arbitration proceed, TKC faces no potential harm which  
 26 cannot later be reconciled or vindicated if a preliminary injunction is granted.  
 27 Should the court ultimately determine that the "expedited" arbitration provision is

1 in fact lawful and enforceable, TKC can promptly reschedule the proceeding to take  
2 place on an "expedited" basis. TKC has adequate and available remedies for any  
3 delay and can seek (and is seeking) interest on any monetary award that it may  
4 ultimately receive, if any. Moreover, TKC has demonstrated that time is not "of the  
5 essence" as the "Personal Guaranty" has been in effect for several years, but TKC  
6 has just recently decided to pursue Mr. Kayne under this premise. *See* Complaint,  
7 ¶42, Kayne Dec., ¶ 3, Coleman Dec., ¶ 3 and Exhibit 2 thereto (containing TKC's  
8 assertion that the underlying "debt" being pursued was incurred in 2002). Any  
9 incremental delay in the scheduling of the arbitration until the completion of Mr.  
10 Kayne's lawsuit will not bring TKC any significant harm.

## 2. Public Policy Favors A Preliminary Injunction

12 As codified in California Civil Code sections 1667 and 1670.5, California has  
13 a strong public policy against the enforcement of illegal contracts or unconscionable  
14 clauses contained in contracts. Therefore, it is in the interest of the general public  
15 that this Court determine the legality of the "expedited" arbitration provision.  
16 Similarly, it is in the public's interest that TKC not be allowed to exercise or enforce  
17 the provision embedded in its form contracts against Mr. Kayne, other franchisees,  
18 or the general public, until a full adjudication regarding the legality of the provision  
19 has been completed.

## 20 | IV. CONCLUSION

21 *Nagrampa* and its progeny now make it clear that it is for the courts, and not  
22 the arbitrator, to determine whether an arbitration clause is unconscionable and  
23 hence unenforceable. If the clause is unconscionable, so too is the result of any  
24 arbitral award resulting from the application of such a clause over the timely  
25 objection of the adversely affected party.

26 Mr. Kayne has a strong interest in confirming, *before* the arbitration occurs,  
27 whether the facially-unconscionable "expedited" procedures in TKC's clause will be

1 deemed to pass muster under *Nagrampa*, *Davis*, *Gentry* and other recent cases in  
2 California and the Ninth Circuit addressing this issue. TKC will necessarily have  
3 to face this issue sooner (before the arbitration) or later (after it seeks to confirm  
4 any arbitral award) based on the tainted "expedited" procedure. TKC can claim no  
5 real prejudice by having the issue presented and resolved now rather than later.

6 For each of the reasons identified above, Mr. Kayne respectfully requests that  
7 this Court grant his motion for a temporary restraining order and preliminary  
8 injunction. Proposed forms of order accomplishing this are filed concurrently with  
9 this motion.

10 Dated: October 1, 2007

Respectfully submitted,

11 HOLLAND & KNIGHT LLP



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